197227

SLOVER & LOFTUS
ATTORNEYS AT LAW
1224 SEVENTEENTH STREET, N.W.
WASHINGTON, D. C. 20036

WILLIAM L. SLOVER
C. MICHAEL LOFTUS
DONALD G. AVERY
JOHN H. LE SEUR
KELVIN J. DOWD
ROBERT D. ROSENBERG
CHRISTOPHER A. MILLS
FRANK J. PERGOLIZZI
ANDREW B. KOLESAR III
PETER A. PFOHL
DANIEL M. JAFFE

TELEPHONE:
(202) 347-7170
FAX:
(202) 347-3619
WRITER'S E-MAIL:
kjd@sloverandloftus.com

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The Hon. Vernon L. Williams
Secretary
Surface Transportation Board
Case Control Unit
Attn: STB Ex Parte No. 582
1925 K Street, N.W.
Washington, D.C. 20423-0001

Re: Ex Parte No. 582, Public Views on Major Rail Consolidations

Dear Secretary Williams:

Enclosed for filing in the above-referenced proceeding are the original and 10 copies of the Comments of the State of New York. Also enclosed is a 3.5-inch diskette containing the text of this letter and the enclosed Comments in WordPerfect 8.0 format.

Please acknowledge receipt of the enclosed filing by stamping and returning to our messenger the enclosed duplicate of this letter.

Sincerely,

Kelvin J. Dowd

KJD:cef
Enclosures

BEFORE THE
SURFACE TRANSPORTATION BOARD

In The Matter Of:	)	
PUBLIC VIEWS ON MAJOR RAIL CONSOLIDATIONS	)	**Ex Parte No. 582**

COMMENTS OF THE
STATE OF NEW YORK

William L. Slover
Kelvin J. Dowd
Peter A. Pfohl
Slover & Loftus
1224 Seventeenth Street, N.W.
Washington, D.C. 20036
(202) 347-7170

Attorneys and Practitioners

OF COUNSEL:

Slover & Loftus
1224 Seventeenth Street, N.W.
Washington, D.C. 20036

Dated: February 29, 2000

BEFORE THE
SURFACE TRANSPORTATION BOARD

In The Matter Of:	
PUBLIC VIEWS ON MAJOR RAIL CONSOLIDATIONS	**Ex Parte No. 582**

COMMENTS OF THE
STATE OF NEW YORK

The State of New York, acting by and through the New York State Department of Transportation ("New York"), submits its comments in response to the Board's Notice in this proceeding served on January 24, 2000.

New York's comments regarding the rail merger policy issues raised in the Board's Notice are presented through the Verified Statement of John F. Guinan, Assistant Commissioner for the Office of Passenger and Freight Transportation of the New York State Department of Transportation, which is attached hereto.

Respectfully submitted,

THE STATE OF NEW YORK,
ACTING BY AND THROUGH THE
NEW YORK STATE DEPARTMENT OF
TRANSPORTATION

By: William L. Slover
Kelvin J. Dowd
Peter A. Pfohl
Slover & Loftus
1224 Seventeenth Street, N.W.
Washington, D.C. 20036
(202) 347-7170

Attorneys & Practitioners

OF COUNSEL:

Slover & Loftus
1224 Seventeenth Street, N.W.
Washington, D.C. 20036

Dated: February 29, 2000

VERIFIED STATEMENT OF
JOHN F. GUINAN

Assistant Commissioner for the
Office of Passenger and Freight Transportation
New York State Department of Transportation

My name is John F. Guinan, and I am Assistant Commissioner for the Office of Passenger and Freight Transportation of the New York State Department of Transportation. I was appointed to my position by Governor George E. Pataki. Among other things, I have managerial responsibility for implementation of all policies and initiatives of the State of New York in connection with rail and motor carrier freight transportation to, from or within the State.

I have had the privilege of representing Governor Pataki and the people of New York in matters related to federal rail policy on a number of prior occasions, including proceedings before the Board to consider the acquisition and division of the former Conrail system (Finance Docket No. 33388) and the state of rail access and competition (Ex Parte No. 575), and hearings before the U.S. Congress to support reauthorization and full funding of the STB. I am offering this Statement in order to present New York's views regarding the impact of recent, major consolidations in the North American railroad system and the policy considerations that should shape the STB's approach to any new proposals for mergers or other transactions that further would alter the structure of the industry.

Background

New York's long history of commitment to the development and preservation of a sound, efficient and competitive surface transportation system is a matter of record. From the public financing of canals in the 1800s to efforts to rescue Conrail's predecessors and nearly $1 billion in rail infrastructure investment over the past 25 years, New York's credentials in the U.S. rail transportation policy debate are well-established. Our commitment continues in this new millennium, particularly in the enhancement of inter-city passenger rail service and the promotion of more effective co-existence and coordination between passenger and freight railroad operations. Governor Pataki's proposed Executive Budget for fiscal year 200-01 includes $80 million in direct investment funds and tax-related reforms dedicated to rail projects and facilities improvements. Through decades of changes in law, commerce and technology, New York has remained at the forefront of State-sponsored rail investment and public-private partnerships.

Among the many changes that have affected the U.S. rail industry and those that depend on it over the past 30 years, by far the most consequential has been the steady trend toward consolidation and rail market concentration. Today, there are fewer major railroads operating in the entire country than operated in New York in 1968. To be sure, many of these changes unquestionably benefitted the public; there was a time when the U.S. simply had too many carriers and too much associated inefficiency to be sustainable, and the heavy hand of federal regulation often stifled innovation and penalized productivity improvements. Particularly in light of the recently-approved division of Conrail and the proposed union of the Canadian National and Burlington Northern Santa Fe systems, however, the modern rail merger trend also presents formidable challenges for States such as New York and their many, rail-dependent constituencies. The risks associated with unchecked railroad consolidations are well-known: a deterioration of service quality as costs rise; the threatened loss of service to marginal markets; the neglect of markets that are not considered part of the carriers' "core" business; and the effective rationing of limited capacity resulting from a lack of private infrastructure investment. As most industries with high entry barriers are not self-policing in this regard, it often falls to the States and federal government to lead in the promotion and protection of the interests of rail consumers, smaller carriers and communities.

Against this backdrop, New York commends the Board for initiating this proceeding to solicit public input regarding the policies that should guide the agency's approach to pending and future rail merger and restructuring proposals. In the balance of my Statement, I will focus in greater detail on New York's experience in the wake of the most significant, recent railroad consolidation transaction - - the Conrail division - - and outline the principles that we believe should be central to the evaluation of any new, major transactions.

New York's Experience With the Conrail Division

As the Board is aware, New York was an early and major participant in Finance Docket No. 33388. Advancing interests and priorities that were identified through a series of public hearings held around the State, New York presented extensive evidence in support of its petitions for various conditions on the Board's approval of CSXT and Norfolk Southern's plan for the acquisition and division of Conrail. The common theme of those conditions was the remediation of adverse impacts of the CSXT/NS plan on New York shippers, smaller carriers and communities. They included the following:

* The restoration of competitive rail freight service to New York City and counties East of the Hudson River.
* The expansion of rail competition and service options for shippers and communities in the Buffalo area.
* The preservation of contract rights and investment recovery arrangements that had been negotiated over the years between the State and Conrail.
* The protection of interchanges crucial to the viability of shortlines operating in New York, and

the removal of unnecessary barriers to competitive shortline interchanges with larger carriers.

* The preservation and restoration of essential rail lines serving New York's Southern Tier region.

* Protection for captive rail shippers who otherwise might be at risk for rate increases to cover the multi-billion dollar premium that CSXT and NS proposed to pay for Conrail.

* Assurance of CSXT and NS' cooperation and coordination with the State's ongoing passenger rail service upgrade and expansion program.

To varying degrees, the State was successful in securing most of these conditions, either through negotiations between the carriers and directly affected parties (such as the Southern Tier West Regional Board), or in orders and prescriptions included by the Board in its final decision. On balance we were optimistic that as modified and conditioned by the Board, the Eastern rail system restructuring represented by the Conrail plan would offer enhanced opportunities for New York shippers and communities, and generally would be consistent with the State's long-term rail policy vision.

Beginning shortly after the Conrail "split date," my Department instituted a coordinated effort involving a number of other State agencies and organizations - - including the Departments of Agriculture and Markets, and the New York Public Service Commission - - to gauge the impact of the transaction on the State and nearby regions. I personally participated in most of these meetings, and some regions, such as Western New York and

Buffalo, also were visited by STB Members and staff. Initially, our review showed service inconsistencies, capacity constraints and other problems that were inconsistent with the expectations of operating cost savings, efficiency improvements and motor carrier traffic diversions that were advanced by CSXT and NS and accepted by the Board in approving the transaction. For example:

1. Many shippers reported experiencing unreliable service, poor communication, and high expenses for car delays and demurrage. Despite representations that large portions of the New York City and East-of-Hudson markets would be won over to rail, motor carrier volumes increased.

2. Shippers with no alternative to rail reported a worsening of conditions, and in the midst of an overall economic expansion, several companies in Western New York curtailed shifts at their manufacturing plants due to shortages of rail-delivered raw materials. One electric utility nearly exhausted its stockpile of coal as result of train delays and yard congestion in Pennsylvania, and Waste Management of New York reported serious delays in moving municipal waste containers via CSXT from Harlem River Yard in The Bronx to landfills in Virginia.

3. New York shortlines complained of interchange delays and inconsistent line haul service, with some perceiving discrimination in the level of service available to their off-line customers as compared to competitors located on the major carriers' main lines. The end result was a loss of competitive

traffic to motor carriage, with attendant consequences for road congestion, fuel consumption and increased air pollution.

4. Across the State, representations regarding infrastructure investment or capacity expansion that were made on the record during Finance Docket No. 33388, or in settlement of claims raised in that proceeding, were going unfulfilled. One example is the rehabilitation of CP Draw, near Buffalo. Before the Board, CSXT and NS pointed to this improvement as a major benefit for Western New York rail users. In the wake of the Board's approval, however, the carriers began insisting that public funds be provided for the CP Draw upgrade. Similar problems complicated implementation of the Board's pro-competitive East-of-Hudson trackage rights condition.

In response to these challenges, New York actively engaged the involved carriers, shippers, communities, and the Board in various efforts to find progressive solutions. To a significant extent, these efforts resulted in meaningful improvements in a number of areas most affected by the fallout from the integration of the former Conrail lines into the CSXT and NS systems. For example:

1. Through vigilant monitoring by the State and the timely attention of the Board in response to filings by New York and the Canadian Pacific Railway, an environment was created which enabled CSXT and CP to reach agreement on practicable terms

for shared access to the rail facilities serving New York City and the communities East of the Hudson River.

2. The Department convened the New York Freight Rail Council, comprised of rail carriers, representatives of various public agencies, and the New York State Business Council, to provide a forum for exchanging views regarding railroad capital requirements, infrastructure improvements, shipper service quality and public resource priorities. Among other things, the Council has helped to foster an atmosphere of mutual cooperation in addressing rail service problems, in lieu of more formal, adversarial courses.

3. We have begun to see a general improvement in rail service quality throughout the State, including a recovery of coal stocks by New York electric utilities and the restoration of transit times and car placement schedules to levels more consistent with those experienced prior to the Conrail division.

4. The carriers have begun to follow through on promised investments in key areas of the State, including NS' $12 million investment in upgrading the Bison Yard in Buffalo, and CSXT's double-tracking project along the West side of the Hudson south of Albany.

Certainly, problem areas still remain, such as the continuing controversy over CP Draw, the service deficiencies still affecting Waste Management and other East-of-Hudson shippers, and the continued reluctance of the freight carriers to follow through on their agreements with the Empire State Passenger Association and other entities regarding the expansion and improvement of inter-city passenger service in New York. Overall, however, timely and selective State intervention has paid positive dividends in improved service and improved relations between New York and its traditional constituencies, and our newest major corporate citizens.

New York believes that the lessons of its own activism in identifying and addressing issues and opportunities arising from the acquisition and division of Conrail should inform the Board's before-the-fact scrutiny of any new rail consolidations that may be presented for federal approval. As the Board recognized in the Conrail transaction and reflected further in its January 24 Notice in this docket, the North American rail industry profile is much different today than it was even ten years ago. It is only logical that federal regulatory policy toward future mergers evolve accordingly.

Policy Guidelines for Future Transactions

New York believes that if any further, major restructurings in the North American rail industry are to be considered seriously, the Board must continue the trend seen in its handling of the Conrail division in modifying and expanding the manner in which it exercises its legal responsibility to review and condition approval of these transactions. Our recommendations in this regard are summarized below, and include New York's views regarding the specific issues of timing, "downstream" responses and financial considerations raised in the Board's January 24 Notice.

A. Continue to Pursue a Proactive Conditions Policy

Until the Conrail proceeding, it seemed that the Board and its predecessor's principal rail merger evaluation standard called for measuring prospective improvements in railroad efficiency (usually as determined by the applicants themselves) against expected reductions in competition between specific shipping points. Most modern mergers passed this test, and approval decisions typically incorporated only those conditions that the applicants signaled were acceptable. In the Conrail case, however, the Board began to expand the scope of its conditions, and imposed several that not only were opposed aggressively by CSXT and NS, but also addressed competitive problems that to some extent transcended the specific rail system changes proposed by those carriers in their application. Examples include the directive that rail markets East of the Hudson River be opened to effective, dual carrier service, and the dismantling of an interchange barrier which unduly restricted the options of the Livonia, Avon & Lakeville Railroad in Rochester.

New York believes that the Board should continue and expand this policy trend in reviewing any future rail merger or consolidation proposals. With only six major carriers left operating throughout the United States, the Board cannot limit its regulatory scrutiny and intervention to restraining railroad excesses. It must move creatively to seek out feasible opportunities to increase or enhance competition in markets affected by a proposed transaction, whether or not it already exists there or would be eliminated by the transaction.

B. Enforce Applicants' Representations

Claims of efficiency improvements, service enhancements and operating cost reductions often have been used to justify a finding that a particular merger was consistent with the public interest, notwithstanding concerns over losses of competition or diminished service resulting from line abandonments and other system rationalizations. Unfortunately, those claimed benefits often have not been realized, or the post-merger reality turns out to be the converse of the pre-merger promise. When this occurs, shippers, smaller railroads, States and communities face risks of increased costs, service degradation, and pressure to use public funds to support infrastructure improvements to expand capacity or restore pre-transaction service levels.

New York is not averse to making investments in rail infrastructure in the interests of improved safety or economic development. Our State's long record of support for Conrail and its predecessors speaks for itself. However, public resources - - be they subsidies, tax relief, loan guarantees or consumer revenues - - should not be looked upon as a failsafe to implement a private merger agreement or simply return service quality to pre-merger levels. New York supports a rail merger evaluation policy that will ensure that where particular service improvements, cost reductions and anticipated efficiencies are used to justify approval of a merger, the burdens of failing to achieve them are not simply passed through to the public in the form of rate increases, service curtailments or rationing, or demands for public investment as pre-conditions to infrastructure improvements. In the same regard, the Board should aggressively enforce its typical oversight conditions, to make sure that merger applicants' commitments to shippers, communities and other constituents are fulfilled according to their terms, and not deferred or watered down as the applicants' priorities shift.

C. **Changes in Rail Systems Affect More Than Rail Service**

When rail systems merge or are consolidated in some other fashion, the impacts extend well beyond rail rates and the quality of service to individual shippers. For example, changing alliances between rail carriers affect affiliations with terminals and ports, and post-merger shifts in rail traffic routings and gateways have implications for everything from traffic congestion in urban areas to the adequacy of grade crossings and crossing safety equipment. New York in particular has experienced both effects. As the Board looks at the "downstream" effects of a merger such as that proposed by the Burlington Northern Santa Fe and Canadian National systems, its focus must extend beyond the impacts on other railroads and their customers to include related transportation industries and facilities, many of which are publicly funded or otherwise intertwined with State and local government services.

It is generally acknowledged that the railroad industry is characterized by heavy capital requirements and major assets investment, increases in which are not always supported by the private financial community. Published reports of Wall Street unease with recent U.S. railroad capacity expansions at the same time that railroad CEOs speculate about rationing limited system capacity paints a picture of an industry that may be reluctant to make the kinds of infrastructure investments that will be required in the aftermath of any new mergers or system consolidations. Coupled with revenue losses from traffic which diverts to motor carriage in response to merger-related service problems, this prospective capital deficit will increase pressure on States such as New York to commit public resources to support needed freight rail facilities.

Unlike highway improvements, there is no meaningful federal role in sharing the burden of public rail infrastructure investment. In reviewing any new rail merger proposals that may be presented, it is critical that the Board not limit its consideration to the capital requirements associated with the projected, optimal system. Applicants also should be required to make a showing that they have adjusted their expectations for contingencies that history shows reasonably may be anticipated, and have incorporated the impact of these contingencies into their capital plans.

D. Proceeding Schedules Must Allow Adequate Public Review and Input

New York's fourth concern relates to timing. In recent rail merger proceedings it has appeared that the Board sometimes has been unduly deferential to the applicants' requests for expedited hearings and strict procedural deadlines at the expense of affording interested parties a full and adequate opportunity to probe the justifications for the subject transactions and present their perspectives and views of the evidence to the Board. Particularly in light of the recent changes in the exercise of its merger review authority that the Board has adopted and New York believes should be continued, there should be a re-evaluation of the procedural schedule template that the Board has tended to follow in recent years.

New York respects the interests of prospective rail merger partners in securing a determination as to the merits of their transaction as promptly as practicable. Complex financing arrangements often hinge on the progress of the Board's processes. However, the fundamental purpose of the Board's jurisdiction in this area is to consider whether a particular transaction is in the <u>public</u> interest; where an appropriate respect for the importance of meaningful public input clashes with the aspirations of the applicants, those aspirations necessarily must give way. At a minimum, therefore, the Board should avoid any presumptions that a longer procedural schedule somehow prejudices applicants' rights, or that once a schedule is set, changes in individual components cannot be considered absent some compelling showing of need. In short, the Board should accommodate procedural schedules to the needs of the affected, commenting public, not the other way around.

Conclusion

The rail mergers and consolidations that have taken place over the past decade have redrawn the map radically, and imposed new challenges on rail carriers, shippers, States, communities and other constituencies for whom efficient and economical rail service is critically important. Many of these challenges have caused some to raise questions whether any further restructuring of the North American rail industry can be approved consistent with the public interest. New York is not among those who would answer those questions in the negative. However, the changes that have taken place since 1990 compel the Board to continue to adapt its rail merger review policies consistent with the principles that I have described, to better balance the many public interests that would be affected by any new rail restructuring proposal.

VERIFICATION

State of New York)
)
) ss:
)
County of Albany)

John F. Guinan, being duly sworn, deposes and says that he has read the foregoing Verified Statement, knows the contents thereof, and that the same are true as stated to the best of his knowledge, information and belief.

John F. Guinan

John F. Guinan

Subscribed and sworn to
before me this 28
day of February, 2000.

Charlotte Belak

Notary Public

My Commission Expires: 1-31-2001